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(a) Unnecessary, because the end of good management sought can be more simply and more certainly attained by other methods.

(b) Unsound, because government should not aim to do for the individual what the individual can better do for himself, and because, with legislation governing the fundamentals of publicity and accountability, the evils which have led to the demand for interference in details will be cured by the almost automatic operation of natural forces—the laws of progress and the effect of competition—which are always to be preferred to arbitrary restriction.

5. That all so-called retaliatory tax laws should be repealed; and that all laws imposing taxation upon life insurance should be so amended that insurance should be taxed, if at all, only to the extent necessary to meet the cost of government supervision; this tax to be levied solely on surplus withheld from distribution (not on reserves or premium income).

DISCUSSION.

MR. ANDERSON: Mr. President, the last speaker (Mr. Johnson) has spoken at considerable length about publicity, limiting himself, however, to general principles. I would like to ask him one or two specific questions.

First, would he be willing to publish the dividend factors used by his company?

Second, would he be willing to put into the policy a table showing how much was collected to defray expenses of management, how much was collected for *cost of insurance*, and how much was set aside each year as a reserve?

MR. JOHNSON: Might I enquire, Mr. President, if my questioner comes from Wisconsin?

MR. ANDERSON: I do.

MR. JOHNSON: The questions indicated as much to me, for they refer to ideas embodied in the report of an Investigating Committee which has been in session in Wisconsin, and which has made recommendations to the Legislature of that State

on this subject which are, to my mind, more impracticable and unsound than any of the many other radical suggestions which have been offered elsewhere. I am accordingly very glad of an opportunity to answer the questions. I judge he desires my view of the desirability of publishing dividend factors and of including in policies issued a table showing the division of the premium between mortality, expense and reserve accounts, rather than an expression of what might be the practice of any particular company in such a matter. What will best serve the interests of the public (which is the question that interests us as economists), is the adoption of such regulations, and only such, as will lead to the granting of sound insurance at the lowest possible cost to the individual policyholder. The object of all insurance legislation should be first to safe-guard the business, to render it absolutely secure, and then to so regulate its conduct that the public will be able to procure all necessary information concerning the conduct of individual companies, and to judge, from the requirement of frequent accountability, which is rendering the best service. Under the rules of publicity and accountability which I have urged, the end sought would be obtained through the operation of natural laws of selection and survival, far better than by an attempted regulation of the details of the business by the State. In my judgment the publication of the factors by which the dividends paid by the Companies are determined, and the printing on policies of tables showing the division of the premium into its elements, not only would not help in accomplishing the end sought, but would confuse a matter which is now none too clear to the average policyholder. The student can readily procure the details referred to from an analysis of the companies' reports or an examination of the tables on which their rates are based. The policyholder is not interested in *how* his dividend is figured, but in *what his dividend amounts to in dollars and cents*, and how it compares with the dividends paid on similar policies by other companies. What affects the policyholder is *the ultimate result*. If that be satisfactory, information concerning the details of operations which lead up to the result will

prove of no interest to the members at large, and they would not appreciate the significance of the various elements entering into the result even if the information were before them. The only ones who would be interested in these elements would be experts and students, who have sufficient specialized training to understand the significance and meaning of the details, and for them, as indicated above, the essential facts are already at hand. The case of the general policyholder may be likened somewhat to that of a sick man laboring under the agony of great bodily pain. He sends for his physician, who comes and prescribes for him, relieving him from the pain and restoring him to health. I take it that the man who is thus suffering acutely, is much more interested in the result, in being promptly relieved, than in the question of how the doctor's prescription may be compounded and whether the drugs used are intended by the physician to act upon the heart, upon the nerves or upon the kidneys. The end sought is relief from suffering, and he would prefer to have it promptly furnished rather than to have the relief postponed while an earnest but impracticable student of medicine delivered to him a dissertation upon the character of the various drugs which would best fit his case and upon the effect which each element of the prescription might have upon the different organs of the body.

Until the day arrives when corporations can be conducted without the intervention of human beings you will find it necessary to consider the human equation even in connection with the management of an insurance company. Corporations differ just to the extent that individuals differ and the exact results attained in the different departments of insurance administration depend largely upon the experience, the judgment, and the knowledge of the individuals charged with the responsibility for the work. Just to show you what confusion the publication of dividend factors might cause to the non-expert policyholder (and the great majority belong to that class) let me refer to the sources from which so-called dividends to policyholders are made up. The rates of an insurance company are based upon a certain table of mortality,

it being assumed that the reserve to be accumulated from the premiums will earn a certain rate of interest, and a reasonable addition being made to the premiums for expenses and contingencies. If through the careful selection of new members, and through the introduction of an adequate number of new lives, the actual mortality experienced falls below that indicated by the table on which the rates are based, there is a saving which may be distributed in dividends to policyholders. If the actual net rate of interest earned by the Company exceeds the rate which it has assumed the reserves will earn, this excess interest is added to the surplus fund and may be distributed in dividends to the policyholders. If the expenses are less than the amounts added to the premiums for expenses and contingencies, then the saving on this account is also available for dividends. There are other minor sources of profit (or loss), such as that which arises from the sale of securities which have appreciated (or depreciated) in value; but it is from the above items chiefly that dividends arise. Now to show you the misapprehensions which the publication of dividend factors might give rise to, and the harm which might be done by such an unnecessary practice, let us consider the case of three different companies, all amply solvent, all possessing the good will and confidence of their policyholders and granting sound insurance at low cost, but all differing in the details of their conduct owing to the human equation which must not be lost sight of in considering and in dealing with this or any other question of an economic nature.

The first Company, we may assume, is one which is very economically managed, in which the expenses fall well within the provision for that purpose in the premiums, thus giving rise to a substantial fund saved for the policyholders and applicable toward dividends. Its economical methods have been accompanied by sound financial management, so that the investments have not only been made without loss, but have netted a rate of interest substantially in excess of that required to maintain the reserves, thus furnishing another contribution to dividend account. The Company, however, because of its extremely economical basis of expenditure, has

been able to procure only a comparatively small new business year by year, and the fresh lives introduced have not been sufficiently numerous to markedly affect the mortality, which has accordingly approximated the table rate. Hence, while there has been a substantial contribution to the surplus fund from which dividends are paid, both from the savings on expense account and the excess interest earned, there has been very little saved on mortality account.

Our second Company, we will assume, has been managed with more freedom of expenditure, which has given less of a contribution to dividend account from expense saving, but which has resulted in the procurement of a much larger volume of new business, the fresh lives introduced leavening the entire mass of policyholders and resulting in a mortality rate well below that provided by the table, thus giving a large contribution to dividend account from mortality saving, a contribution which fully offsets the increase in the expense account over Company Number One. The second Company has likewise been well managed financially so that there has been a contribution to dividend account from excess interest similar to that in the first instance.

The third Company, we will assume, has, owing to a very excellent reputation, been able to get an adequate amount of new business and so have the benefit of a low mortality, thus making a substantial contribution to dividend account, while at the same time keeping its expenses on a very economical basis, this also giving rise to a substantial fund for dividends in the shape of expense saving. It, however, has not been as well managed financially, or through some ill-fortune has had some of its investments turn out poorly (investments very possibly which were originally made thirty years ago by some previous management), and hence instead of the net interest earned exceeding that required for the maintenance of the reserves it has just been sufficient for that purpose, and there is accordingly no contribution to surplus or dividends from interest account.

Now the dividends paid on policies by these three companies are practically identical, and a member of one receives his in-

insurance at just as low a cost as the members of the other two. It, of course, is of value to the Directors and the Officers of each Company to examine the details of their business, the results on the different accounts, etc., and take such steps as may be necessary and possible to strengthen the weak points and bring about ultimately a saving on all three accounts. Yet, of course, it may not be possible to overcome the effect of some early mistaken policy as to investments, for instance, for a great many years to come. There are companies holding in their investment account to-day real properties title to which became vested in them thirty-five or forty years ago through the mistake of some previous management. The properties have been disposed of gradually as opportunity has offered to do so profitably, or at least without too great loss; but the effect of some mistake of this character in the matter of investments may not be fully overcome by a company for a quarter of a century. The facts are also of interest to the student and to the insurance expert, but I cannot see of what earthly value it would be to the average policyholder who had a policy perhaps in each Company, on which the dividends were identical and which were all giving him his insurance at the same cost, to know that in one Company the larger part of the dividends came from expense and interest savings, in another company from mortality and interest savings, and in the third from expense and mortality accounts. It would do the average policyholder no good to require each company to publish the factors used in the computation of its dividends, and would simply arm the unscrupulous with a new method of deceiving and confusing the public. What is needed is to bring out the simple result as to which companies are granting insurance at the lowest cost, and confusing details as to how that cost is arrived at, while of value to the expert and procurable by him upon an analysis of the official reports of the companies, would be of no possible value to the policyholder at large.

My answer on the subject of publishing dividend factors applies in large measure to the proposal that a table be attached to every policy showing the elements into which the

premium is divided, its application to expense and mortality accounts, and the balance of the latter account, i. e., the terminal reserve, left after making provision for current mortality. It would serve no good purpose; it would not avail to reduce the number of deaths, or to increase the net interest earnings, or to lessen the sums, for instance, which the companies are compelled to pay to the States for taxes and which would otherwise go to the policyholders in dividends. It would be just as proper and contribute just as much to the welfare of the public for the State to require the publication of such a table upon insurance policies hereafter issued, as it would be for government to insist upon the publication of a summary of operating expenses on the reverse of every railroad ticket issued, or the furnishing by the Universities every term to each student of a printed statement indicating the proportion of his tuition fee which has been applied to the salaries of the professors, to the maintenance of buildings, and to the purchase of supplies.

Unorthodox as it may seem in this day when the interests of the policyholder appear to have been taken within the especial care of those who lack sound knowledge of or actual experience in the conduct of the business, I venture to say that there is no body of men so keenly interested in any and every measure which will actually benefit the policyholder through a reduction in the cost of life insurance, as the insurance managers themselves, and I can only say that if the laws leave them free to conduct their business efficiently without being hampered by absurd and useless restrictions, but with such publicity and accountability as will enable the public to see year by year the actual results attained, the problems which have been given so much consideration within the last year or two will be completely solved, and you will soon find all the companies conducting the business conservatively, successfully, with due regard to the interests of the policyholders, and with just as great a degree of economy as can be applied without impairing efficiency.

MR. ANDERSON : I was fully aware that my questions would meet with opposition. We had those questions discussed at

the meeting of the general agents in Milwaukee, and I am quite familiar with the objections that have been made against the insertion of such a table in the policy.

I would like to say just another word since the Wisconsin Investigation Committee has been referred to. I feel that I have some interest in the work of that committee, having been in their employ as secretary from the time the work began until it was finished.

There seems to be an impression current in the East that the recommendations of the Wisconsin Committee are unreasonable. I will venture to say that when the report comes from the printer some parts of it, at least, will not appear as bad as the rumors that have been circulated about it. Some parts may be worse. (Laughter.)

I want to correct the statement made by my friend, Mr. Hoffman, to the effect that the Wisconsin Committee rejected everything recommended by the Armstrong Committee. The fact is that the Wisconsin Committee adopted many of the recommendations of the Armstrong Committee, and of the Massachusetts Committee as well.

Perhaps it might not be out of place in this connection to call your attention to the fact that there are three kinds of insurance investigations. First, there is the actuarial or departmental examination made by the various state departments, which concerns itself almost wholly with the question of the solvency of the companies. That is to say, they value the policies and appraise the assets. If the assets are sufficient to cover all the reserve liabilities and leave a working surplus, the company is given a clean bill of health and that is the end of it.

Second, there is the lawyers' investigation, which consists principally of calling witnesses to the stand to determine whether or not there have been any questionable transactions, and

Third, there is the economic and social investigation, which may or may not include both of the other two. Its object is to determine the economic and social efficiency of insurance. That is, to determine what is actually received as benefits for

the premiums paid, as well as to determine whether or not the burdens are equitably distributed among the individual members.

The Wisconsin Committee has gone deeper into the question of insurance from the economic and social standpoint than any other committee ever did. I cannot at this time discuss in detail the data gathered by our committee, but will state very briefly some of the most striking results.

First, there is an appalling amount of social waste resulting from the lapsing of policies before surrender values take effect, as well as from the heavy surrender charges imposed by many companies when policyholders surrender their policies.

Second, the lapses appear to be by far the greatest among the small policies, and this goes to show that the greater part of this social waste is borne by those who are least able to bear it.

Third, panics and hard times have considerable effect on the lapses and surrenders, especially if the policies have been recently issued when the financial disturbance comes.

Fourth, quite contrary to our expectations, and contrary to the contentions of some insurance men, the annual-dividend policies were shown to be much more persistent than the deferred policies, in some cases the difference being over one-third.

Fifth, it appears that the present method of loading the premium to defray expenses is unscientific and grossly unequal as between the individual policyholders having different kinds of policies, and for this reason the committee recommended that the companies be required to show, when the application is written, how much is collected each year for the purposes of expense, cost of insurance and reserve. The plan is entirely feasible; it is perfectly just, for it is publicity of the most effective kind.

I also wish to say that I heartily agree with the views expressed in the first (Prof. Robinson's) paper in its advocacy of federal supervision, because uniformity in the legal requirements is highly desirable, if not absolutely essential, to an

effective control of the business. We can never have uniformity as long as forty or fifty states legislate independently of each other to regulate the same companies.

W. G. LANGWORTHY TAYLOR: By an extension of the term "gambling" it may be made to include all businesses: in all there is an element of risk. However, risk is the most important element in industrial progress. That is to say, all efforts at progress are tentative and all industrial undertakings are, in the nature of things, ventures. Not only may outer nature be unpropitious and mechanical inventions fail when put to the test of wear and tear, but demand may fail to be aroused or may suddenly vanish after it has long been relied upon as a constant factor in the problem. In fact that business which is looked upon as furthest removed from gambling is the one in which there is perhaps the greatest risk, the business of agriculture.

But provided the risk be incurred for the purpose of creating additional values, it is economically praiseworthy and cannot be called gambling, since gambling is a term of moral stigma. The American people is considered to have increased in wealth faster than any other and this is partly because of the well-recognized fact that the American business man is more willing to incur risk than his confrere of any other nationality of equal intelligence and technical attainments. This kind of risk is progressive or incurred in the cause of industrial progress. It does not invite government interference and the presumption in this case is against government regulation, at least according to the theory that enterprise is rather a matter for individual than for government initiative. If government interference becomes necessary it is only in extreme cases and should be minimized. Government interference in the field of competitive business is only in order to secure fair dealing between men; and generally publicity of operations involving the element of equity or trust is the measure of public control. Especially where such vast investments are involved as those made by life-insurance companies, is it generally conceded to be inadvisable in a progressive civiliza-

tion such as ours for government either to take over the business or to hamper the judgment of the persons upon whom such vast interests have devolved.

The simple theory of life insurance, however, involves no such vast accumulations of property as have been made by our insurance companies. The reserves involved in this business do, of course, amount to a large sum, but they are less than the sums actually in the hands of the insurance companies. The risk involved in life insurance is much less than the risk in other businesses. As to the insured, he is sure to die anyhow; the insurance neither accelerates nor retards that event; and the premium is fixed beforehand. Nor does the insurer take so much risk as is taken by the ordinary business man or company, for on a sufficient group of lives the mortality tables give a pretty accurate prediction.

Life insurance therefore in its pure form is perhaps better calculated to be managed by a government office than other business, especially if the government has a debt in which the reserves may be invested in the same way in which deposits in the Postal Savings Banks in France are invested in the French national debt. But there are grave objections to the taking over of life-insurance business in its pure form by government, and fortunately no one is proposing that that be done in this country.

With endowment insurance the case stands very differently. It is not insurance at all but the very antipodes of insurance: the buyer of this risk stands to gain only if he is among a small number of survivors from a larger group. The buyer of pure life insurance buys a legitimate protection and may not have paid too much even though he lives to old age and has accumulated premiums to an amount double the insurance, as occurred in a case with which I am acquainted; but the buyer of an endowment policy is not risking his own death but the death of others. He is gambling on his own survival and on the decease of the other members of his college. It is true that there is little uncertainty to the insurer, since here again the mortality tables apply; nor, since the college of policyholders is a large one, can the insured seek by charm or

incantation to shorten their lives to his own advantage. But he is a stranger to them and he buys an opportunity to inherit their property. Is this a moral and civilized proceeding? Is it desirable from any point of view that the hard-earned savings of industrious men be gambled away to strangers instead of remaining in their own families, where they properly belong after the decease of the head of the family? It is not probable that the endowment principle would have attained such widespread favor if the matter had been put to policy-holders in this way.

Naturally insurance solicitors present the advantages of insurance very differently. Endowment and pure insurance plans are so mixed up in the policy as to be indistinguishable. For a lump sum the prospective insuree is told that he receives protection, and then is agreeably surprised with an additional contract to pay him a very respectable sum at the end of say twenty years and dividends which may have accrued up to that time, or in the most favorable case, dividends payable annually which he may spend or apply on the reduction of his premium or on the increase of his policy. Moreover if he becomes tired of his contract the company will kindly refund to him a part of his premiums already paid and thus share the loss with him. What could be more attractive? And yet if the insuree saw clearly that he could obtain simple protection for a tithe of the stipulated premium, he would think a second time before entering into the more onerous obligation. If he took the surplus and regularly deposited it in a savings bank he would get a larger return than he receives even by trading on the misfortunes of other families, and would not run the chance by his early death of presenting them with a windfall.

The endowment feature is not wholly to be condemned. Great numbers of persons have been induced to make savings who would not have taken advantage of savings banks, and thus perhaps the world is not the poorer for it and may even be richer. The benefit of this form of investment to the improvident reposes of course upon the fact that the investment cannot be withdrawn except at a considerable loss. After the contract is made therefore there is every incentive to continue

premium payments, and thus the endowment principle must have an educational feature in cultivating that spirit of saving which is the great basis of modern prosperity and especially of American prosperity.

From the financial point of view, however, there are serious objections to the plan, which partly counterbalance the educational benefit, in the scales of social utility. Soundness of a great social financial system reposes upon the obligation to pay upon demand. The bank system has grown to its present importance precisely because deposits and notes are payable upon demand. The temporary money stringencies which we continually witness are the sign of the effectual operation of the adjustment of the flow of capital between different localities through the operation of this simple principle. The institution of savings banks is a first step of derogation from this principle; but savings banks have undoubtedly been of more benefit in inculcating thrift than of injury in the immobilizing of capital. The endowment contract, however, immobilizes capital for much longer periods than savings banks. The dangers to which the whole community is exposed from this exaggerated immobilization of vast sums of capital gathered from every hamlet in the land and put at the disposal of vast schemes of financial control, have been clearly brought to light by the investigations of the Armstrong Committee. Enterprise is a good thing but there is such a thing as too much enterprise. Concentrated capital held subject simply to a distant obligation of recall, becomes a tool for raiding methods in finance and for guerrilla warfare between financiers. The country has looked with alarm at the manner in which bold financiers have been able to capture vast enterprises and to combine them into vaster ones by the employment of capital not their own. The pickings of a few insurance officials are a matter of little moment compared with the use of reserve funds collected in money centers for an exaggerated control of industrial undertakings.

This evil will be cured by Time as others have been before. I am informed that there is already a marked tendency on the part of policyholders to reject this feature of insurance.

The solicitation of insurance has been carried much too far. It has been a natural accompaniment of the endowment principle. The possibility of collecting vast sums is in itself very attractive and even though they are to be paid back at a later date, the temporary control of them must give great influence to insurance officials. The vast army of agents is become a vested interest. The proposition to reduce the urgency and insistency of the hunt for possible policyholders is a very serious matter to the agent. It seems to him impossible that life insurance can survive without him; at least he knows he cannot survive without it! But insurance is not the only business in which solicitation has been carried too far. The evils of over-advertising have often been descanted upon. The mails are used to pester the whole community with propositions in mining stocks, patent medicines, and books, craftily couched to catch the unwary. Let us have a partial return towards buying the thing we know we want at the place where we know we can find it!

The evils of over-solicitation have been proved in many different ways. So accustomed are life-insurance men to its necessity that they never question it. Even in straight life insurance they claim that an infusion of fresh lives is necessary in order to keep the average of ages uniform, but this certainly cannot be true if the premium paid by each individual represents its true actuarial worth and if a sufficient number of lives—say a thousand—be included in the group. Beyond a certain number, additional lives add nothing to the actuarial necessities of the case. The endowment principle adds enormously to the desire for further extension of business on account of the unrestrained passion of men for the aggregation of big capitals, while it is notorious that fraternal organizations would have to close their doors very quickly if they could not keep down the assessments by new insurance, and that even new insurance cannot keep them on their feet very long.

Perhaps the best evidence of the illegitimacy of undue solicitation is to be found in the enormous number of lapses, especially in industrial insurance. Thus it is stated in the

Armstrong Report: "It is found that in the Ordinary Department over 44% lapse during the first three years. In the Industrial Department between 62% and 66% lapse in the first three years." (P. 337). Stated in another way, the number of lapses including deaths, which amounted to less than 1%, is found to be as follows:

Within 13 weeks.....	29%
Within 13 to 26 weeks.....	12.8%
Within 26 to 39 weeks.....	5.7%
Within 39 to 52 weeks.....	3.8%

Total within year..... 51.3% (P. 338.)

"In 1905, 1,253,635 Metropolitan and 951,704 Prudential policies lapsed" (Louis D. Brandeis, *The Independent*, Dec. 20, 1906, p. 1478). The same writer says that the Columbia National Life Insurance Company wrote during the year 1905, 103,466 industrial policies. At the end of the year it had outstanding only 63,497; and yet of the 143,863 policyholders only 699 had died, while 79,677 policies—that is 114 times as many—had lapsed." Professor Allan H. Willett states: "Of the business terminated by the four industrial companies in Connecticut during the year 1903 4.41% was terminated by surrender and no less than 90.10% by lapse. This represents an enormous tax upon the resources of the laboring classes." (*Political Science Quarterly*, Vol. 20, p. 471.) The same author states, "The average of regular terminations for 31 companies reporting to the (Connecticut) Department was 35.21% of the total terminations, leaving 64.79% as the share terminated irregularly, of which all but 5% was by lapse or surrender."

Under these circumstances some recourse to state intervention and regulation is undoubtedly indicated. Whether complete prohibition of deferred-dividend contracts is advisable may be open to question. Certainly the policyholder should be notified annually of the exact amount due to him under the existing condition of the company. That requirement would prevent the companies from holding out expectations of important future gain from the investment side of

insurance. Perhaps it is not a bad scheme to restrict taxation of insurance companies to the undistributed surplus of the company; and further than this the utmost publicity of the operations of insurance should be secured.

In the matter of securing publicity the state insurance departments have signally failed. They have rather been agencies for the promulgation of whitewashing reports which have been used by the companies as advertisements for the further spreading of endowment policies. Government regulation should not forbid the spreading of endowment insurance. The general tendency towards centralization of commercial regulation in this country indicates that something should be done towards stimulating the activities of the federal government in the matter of investigation of life-insurance methods and exposure of abuses. The Bureau of Corporations already has the power to investigate life insurance. Let it use that power. If it needs additional money and men for the purpose they will be readily forthcoming when the attention of Congress is called to the matter.

Economically speaking insurance is not commerce. It is finance. The essence of finance is the contract of guaranty; and insurance is plainly a contract of guaranty. But the lawyers are taking care of the constitutional question for us. They are rapidly deciding that insurance is commerce, and for present purposes it makes very little difference on what constitutional theory the requisite powers are given to the central government. It has not been proposed that the central government charter insurance companies but that it be given additional powers in enforcing publicity. Our narrowing contact with foreign countries touches us in insurance as it has touched us already in commerce, in finance, in diplomacy, and even in educational questions. We want to take every means at command to find out whether our insurance magnates are promoting railroad combines and whether they are using insurance funds in participation syndicates, in collateral trust bonds, or in bank accounts A or X.

FRANK E. HORACK: Without entering into the constitu-

tional or legal difficulties to be encountered and overcome before the organization and government control of insurance companies by the National Government can become a reality, I want to emphasize what in my opinion would be the chief advantages of such organization and control.

The fact that the insurance companies themselves are working toward this end is not necessarily against the proposition. Government control will undoubtedly benefit the insurance companies by giving them a uniform and simplified organization. This must mean a considerable economy in management over the present system. Moreover, I believe that if means are found to bring this insurance business within the power of the National Government, it will hasten the movement for the organization and control or the control at least of industrial and business corporations engaged in interstate business.

The insurance business is only one of the great enterprises conducted in corporate form in this country which must sooner or later come under the surveillance of the National Government. President Roosevelt urged national legislation for corporations engaged in interstate commerce in his first message to Congress and this year to the second session of the 59th Congress he again calls attention to the need of securing Government control of those great corporations the operation of which are confined to no one State. The impossibility of securing uniform legislation by State action is apparent to any one who has given the subject the slightest thought.

In my opinion all of the arguments urged in favor of organization and government control of insurance companies may well be applied to all the great corporations engaged in interstate commerce. To sum up briefly, the advantages of Government organization and control are:

1. It will give such corporations a uniform and simplified organization.
2. It will make possible a uniform line of court decisions respecting the powers and duties of such corporations.
3. It will be one of the most efficient means of checking the evil of overcapitalization.

4. It will give better protection to policyholders and to stockholders, particularly in giving them information as to whom their associates are.

5. It will give American companies transacting business abroad a better standing, as well as better protection.

6. It will check excessive profits and reduce the cost of insurance.

7. It will put a stop to the disgraceful traffic in corporate charters for the sake of the fees which the corporations willingly pay for immunities.

8. It will put the standard of corporate legislation in this country on a par with that of England and Germany.

FREDERICK L. HOFFMAN: The address of Professor Robinson before this Association marks an important step in the advance of insurance science as a branch of economics. The observations, on the whole, are sound and in conformity with the facts, and the address illustrates forcibly the value of independent and impartial research work in practical economics. The scientific study of insurance has been almost completely neglected by economists, with the exception of the valuable monograph of Mr. Allan H. Willett and the occasional discussion of its social aspects and importance by Prof. Ely, of Wisconsin. A very promising field lies open to any one, but no more serious error could be made than to assume that all the knowledge and wisdom respecting the business is to be found in the Report of the New York State Legislative Committee, or in the Report of the Special Committee of the Legislature of Wisconsin. Insurance has a wide literature and most interesting history, but few trained minds in economics have given the matter serious concern, and the subject awaits the coming of the master mind which shall successfully differentiate the sound theory from the unsound, and the valuable material from the worthless. In no direction, perhaps, is the value of special research-work on the part of trained economists better illustrated than in connection with the constitutional aspects of the problem of

Federal supervision of insurance, or the specific question whether, under our Constitution, insurance is commerce or an element of commerce within the meaning of the Commerce Clause. Now, while there has been much discussion upon this point, there has been practically no research-work to establish with accuracy the point of view of the early American statesmen from a study of the works of Hamilton and Wilson, the early American State Papers, the debates of Congress, etc., not to speak of the much-neglected field of the actual practice of ancient and modern commerce and navigation.

Much valuable material will be found in the early dictionaries of commerce, and dissertations upon the Law Merchant, maritime law and custom, and even international law contain much that will prove useful and suggestive. In other words, there is urgent need of a comprehensive inquiry into our political and commercial history, to ascertain whether or not in the early debates and discussions, insurance has been considered an element of commerce in the same sense as bills of lading and bills of exchange. It is to be hoped that some earnest student of economics will take up this question and produce a work useful for practical purposes and which would serve as an aid in the successful solution of the pending problems of the relation of insurance to the State.

Not much good, however, is likely to result until the whole subject of insurance is included within the scope of university education and until the science of insurance is taught in the same manner as other applied sciences are now being taught in our great institutions of learning. An excellent beginning in this direction has been made in Germany by the establishment of an insurance seminary at Göttingen, under Prof. Lexis, and of an insurance course in the Commercial High School at Cologne under Prof. Moldenhauer. In so practical a country as America, it is difficult to understand why insurance has not long since attained to the dignity of an applied science and been taught as such in our universities. By such teaching I mean more than the actuarial branch of the business of life insurance, for I would make the instruction include every department of the business, or, in other words, represent insur-

ance science in the true and complete sense of that term. The division is natural into different sections—such as, first, the economics and theory of risk and insurance; second, the history and literature; third, the law of insurance, both private and administrative, including State supervision and control; fourth, the mathematics of insurance, or the practical application of the doctrine of probability; fifth, the finance of insurance, including the doctrine of interest; sixth, the administration of insurance companies, including the science of accounting; seventh, insurance medicine, including hygiene and diseases of occupation; eighth, the business of insurance in practical life, or its social aspects, including statistics, comparative experience, social utility, etc.; ninth, insurance technology, including insurance engineering, prevention of fire waste, etc.

If some such comprehensive plan were introduced into one or more of our leading universities, in place of the present more or less inadequate method of instruction, and if the co-operation of the companies were enlisted to secure material and data, literature and forms, etc., the step would mark the beginning of a new era and the result would be to substitute facts and truth for error and guesswork, and the benefit to society and the State would be incalculable.

F. A. CLEVELAND, PH. D.: The papers read and the discussion following seem to be practically in accord in their advocacy or deferential acceptance of the principle of publicity. That is to say, the need for state control over insurance companies is accepted and publicity is held a necessary incident thereto.

Advocating publicity, Mr. Johnson, in his excellent paper on "The principles which should govern the regulation of life-insurance companies," contrasts the almost complete absence of regulatory acts in Great Britain with the voluminous State insurance legislation in the United States, and concludes that the one provision—"publicity"—in Great Britain has given a complete solution of the problem of regulation, while America with all her statutes—inquisitorial, restraining and

mandatory—has been periodically wrapped in scandal, and both policyholder and insurance company have suffered greatly from an inefficient form of control.

“The statutory provisions covering the operations of life insurance companies in Great Britain (since the adoption of which they have been particularly free from cause for criticism) are embodied in the ‘Life Insurance Companies’ Act, 1870.’ The framers of the Act aimed at allowing the companies full freedom in their conduct of business, while compelling them to make public the results of the operations.” This is the *resumé* given by Mr. Johnson of the English situation. His interpretation of legislative motive is that the English people believed that *publicity would do more to secure sound management* than any other method which might be adopted.

The conclusion reached by Mr. Johnson seems to be well supported by experience, not only by the experience of insurance companies, but also by English practice with respect to every form of corporate activity and executory trusteeship. From his reasoning, however he has omitted an important feature of the English Statute Law, viz the “Companies’ Acts.” requiring an independent audit of all corporations registered under the act of 1860, and specific Acts requiring the audit of Savings Societies, Friendly Societies, Railway Companies, Water, Gas and Electric Lighting Companies, etc. While the Act of 1870, regulating life insurance did not make obligatory the appointment of independent auditors by stockholders, (or in mutual companies, by policy-holders,) and the Companies’ Act of 1890 includes only such insurance companies as were registered under the law of 1862, the defect in the law is effectively cured by an enlightened public opinion requiring financial statements to be certified to a basis of credit and public faith. One authority comments as follows: “This [the failure to impose the duty of an independent audit] was certainly a grave omission, and will no doubt be rectified in a future Act, as there is no class of company which so imperatively demands a strict investigation of its accounts. It is true, however, that nearly all life-insurance companies have auditors.”

The English law above referred to is the result of the investment losses and scandals which occurred in the early part of the eighteenth century. Between 1840 and 1870 Parliament had enacted numerous measures for the protection of stockholders and other investors, an essential provision of which was that the stockholders at their annual meeting (when officers are elected) shall appoint an independent auditor. These auditors as the representatives of stockholders and beneficiaries were given access to all books, records and files kept by the officers and trustees of the Company and were held civilly and criminally responsible for the truth of financial statements made. Such companies as do not specifically come within the statutes find it to their advantage to have the certificates of auditors on their statements.

This general practice supplements the specific requirements that corporations shall report to the Board of Trade. The independent audit, as a function of control, is seldom touched on in discussions pertaining to the regulation of corporations; Professor Robinson's paper is among the few that have drawn attention to the relations of an audit to the problem of public control. If there is anything to be added to what has been said it is along this line.

The contrast between the English method of control and the American is pointed. England throws the primary burden of control on the stockholder or beneficiary, and by law provides the means necessary to its enforcement. To restate the provisions of English law, it requires: (1) that stockholders shall appoint a representative to inform them as to the manner in which the corporate estate which is in the possession of officers and trustees has been managed and to report on the conditions of the trust, thus placing in the hands of stockholders and beneficiaries a non-partisan statement which may be used as a basis for protecting the rights and equities of parties in interest; (2) that the officers shall make a full report to the Board of Trade.

In the United States we have followed the Continental practice. We have assumed that the Government is the guardian of the stockholder. Having a democratic gov-

ernment, instead of adopting the democratic rule of self-help which prevails in England, we have assumed that it should become paternalistic. Even in Germany and Russia, where paternalism has advanced to a point which we cannot hope to attain, government regulation has proved less effective than private regulation in England where the law requires the stockholders and the trustees to inform themselves, through their own auditor, as to the conduct of affairs.

Let us be more concrete and consider corporate conditions as they were found to exist in our insurance companies. The recent investigations have proved: (1) that for years there has been wholesale speculation and subversion of funds; (2) that during this time the companies have been under constant scrutiny by departments of insurance of every state in which these companies have done business; (3) that in nearly every instance the public officer has faithfully executed the law governing his office.

What has been wrong? The wrong has lain in expecting of the public officer something that was not intended or, under the statute, was not included among his duties. The public officer was created to protect the public against loss from insolvency. The Superintendent of Insurance, like the Comptroller of the Currency, is to perform the duty of policing the corporations in order that the public might not suffer from the impairment of capital or loss of funds which by law are required to be kept as reserves for meeting outstanding obligations. This duty might be conscientiously performed and yet millions of dollars might be wasted by the companies through inefficient or extravagant administration.

Let us look more closely to the practices of companies which have been made the subject of criticism and consider whether or not these practices come fairly within the purview of public regulation, or if so whether the public officer is the one to apply the remedy. The causes of complaint may be summarized as follows: (1) There was no adequate method whereby the administrative officers of the company might know whether all of the income accruing to the company had been realized, and consequently no adequate administrative

control over the collecting agents; (2) there were expenditures amounting to millions of dollars per year over which there was no adequate audit or accounting control; (3) in some instances, even such audit as was provided for by the Company was from three to four years behind—i. e. the insurance companies were doing just what the United States Government is doing to-day, viz.: paying claims against them, then auditing these claims later, seeking to hold the disbursing officer responsible; (4) as a result there accumulated on the books as “unadmitted items” hundreds of thousands of dollars, which, though stated as assets under the head of “due from agents,” were lost to the company and thereby were diverted from possible use as dividends; (5) supplies amounting to hundreds of thousands of dollars per annum were purchased at exorbitant prices, and in some instances, at least, with collusive intent; (6) salaries were arbitrarily raised far above the value of services received; (7) there were loans to friendly interests at rates below the market, in the form of call loans and deposits; (8) there was subversion of funds by agents for private or improper purposes; (9) there was lack of co-ordination between different departments of the service and the consequent loss in administrative efficiency; (10) there was lack of intelligence on the part of those in positions of official responsibility as well as on the part of the board. Generally speaking the whole situation may be summed up in the statement that there was a lack of intelligent administrative and directive control over the business by officers and by the Board.

The administrative side of the corporate problem has never been appreciated either by officer of state or by publicist. Few, if any, of these situations might be reached by any system of direct public control. These are administrative questions and situations, to reach which the government must either assume a complete direction of affairs or, as is done in England, require that the stockholders shall annually inform themselves by their own chosen representative as to what is being done by officers and trustees, and require, further, that the administrative officer shall report fully to the state.

In Massachusetts it has been proposed that a public accountant shall be employed as auditor, but that his employment shall be by the Superintendent of Insurance. This provision could have nothing more than a restraining effect. No action might be taken by a public officer except such as would be in the nature of police regulation. The state cannot assume to judge for stockholders and trustees as to whether an employee is rendering efficient service, whether his salary is greater than it should be, whether the quality of goods is sufficient for the purpose intended, etc., etc. Questions of economy and efficiency are for the administration to consider and for those who are interested in administrative results.

It is in this relation that the regulative superiority of the English law may be seen. The annual audit by a representative of the stockholder or policyholder is a critical examination which takes into consideration administrative questions. The report of the auditor is to the share-proprietor of the business or to his direct representatives, the trustees. The public accountant not only has to do with the protection of the estate, as has the public officer, but also he goes into every relation of economy, efficiency, operative result and financial condition in which the proprietor himself or the officer is interested. He is the personal representative of the proprietor and the professional advisor to the officer and trustee on matters of administration. The public examiner on the other hand is an advisor of a department of state. His examination can be of little aid either to officer or trustee, and can give little information to the proprietor. The report of the public accountant goes at once to the share-proprietor or to his direct representatives, the trustees, who may correct abuses. The report of the public examiner, if it may contain the same information, goes to the public officer, who may consider it only from the point of view of public control. He is not in a position to consider or act on matters of official judgment. Regulation by the state at best cannot reach questions of administrative discretion.

English experience has taught us that the best police regulation over an agent or trustee is to keep his acts constantly

before his principal, who may find a remedy in the courts for any and every breach of faith, and who has an even more effective remedy in his right to dismiss agents for failure to exercise good judgment in the management of his affairs. For either remedy the proprietor or beneficiary has placed in his hands the evidence necessary to its intelligent accomplishment.

Mr. Johnson announces "that the fundamental principle upon which all sound governmental regulation of life-insurance companies should be based, is the requirement of (1) *complete publicity concerning their operations* accompanied by (2) *a detailed and frequent accountability* for all surplus and other funds." He has shown that these two principles are operative in England which makes little provision for their enforcement, while with all our laws they are inoperative in the United States. Professor Robinson in his paper has suggested the salient feature of the English law which makes it effective. There cannot be complete publicity unless a critical examination is made, both with respect to compliance with law and with respect to administrative economy and efficiency; there can be no effective results from publicity unless the whole financial and operative situation is placed before both the state, the stockholders and policyholders. "Complete and frequent accountability" can come in no other way; it can never come through a public officer except under a system of government ownership. The last principle suggested by Mr. Johnson, *official character*, can be made effective only where there is a direct official responsibility enforced by the share-proprietor or trustee. This also, in a corporation where the share-owners or beneficiaries are widely scattered, can come only after a critical examination by a professional advisor to parties in interest.

The present trend of legislation is to add more restrictive and mandatory legislation to that which has already proved ineffective. The best regulation possible to business is to place in the hands of parties in interest data which will enable them intelligently to judge as to the manner in which their affairs are being managed. This can best be done by means

of a compulsory audit by a representative of the proprietors and beneficiaries—by one who for purposes of examination and report is made superior to the officer and trustee. The necessity for making an audit compulsory is to insure that the report shall go to the real parties in interest instead of being buried in the archives of state or concealed from view by the officers whose acts are being reported. The necessity for making the auditor civilly and criminally responsible is to make the responsibilities of an examination so great that one not trained to this character of advice cannot afford to take the risk of certifying to statements of financial condition and current operative results. By requiring a statement of affairs under such penalties and liabilities, and subject to review by officers of state charged with the enforcement by law, both public control and private control over insurance companies will be made most effective.